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## Working Conditions, Work Outcomes, and Policy in Asian Developing Countries

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## Working Conditions, Work Outcomes, and Policy in Asian Developing Countries

### Abstract

Developing country labor practices and the working conditions that result from them are both generally poor and increasingly drawing attention from governments, corporations, and the popular media. This review provides an introduction to some of the leading academic literature and ideas that are important for understanding the persistence of poor labor practices and possible policies to address these conditions. The literature is reviewed with the goal of moving from the root causes of poor conditions to innovative solutions. Several such solutions, such as the Better Work program, are discussed.

### Keywords

apparel, personnel economics, working conditions

### Comments

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# WORKING CONDITIONS, WORK OUTCOMES, AND POLICY IN ASIAN DEVELOPING COUNTRIES

*Raymond Robertson, Hongyang Di, Drusilla Brown, and Rajeev Dehejia*

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## ABSTRACT

Developing country labor practices and the working conditions that result from them are both generally poor and increasingly drawing attention from governments, corporations, and the popular media. This review provides an introduction to some of the leading academic literature and ideas that are important for understanding the persistence of poor labor practices and possible policies to address these conditions. The literature is reviewed with the goal of moving from the root causes of poor conditions to innovative solutions. Several such solutions, such as the Better Work program, are discussed.

*Keywords:* apparel, personnel economics, working conditions

*JEL codes:* F66, J8



## I. OVERVIEW

Developing country labor practices and the working conditions that result from them are both generally poor and increasingly drawing attention from governments, corporations, and the popular media. This review provides an introduction to some of the leading academic literature and ideas that are important for understanding the persistence of poor labor practices and possible policies to address these conditions.

This review pays particular attention to labor practices in Asia's apparel sector. Asia gained a significant amount of global apparel production following the end of the Multifibre Arrangement (MFA) in 2004. With the increase in production came renewed attention to the conditions workers experience while producing apparel that is largely exported to developed countries. Apparel is important for several reasons. First, apparel is often seen as one of the first steps in the process of economic development. Second, in most countries, most workers are women and it is becoming increasingly well understood that the rights and working experience of women play a critical role in economic development. Third, for many countries, "globalization" has deep ties to the apparel industry because in many emerging Asian economies, their exports and foreign investment are related to apparel.

The term "working conditions" is broad and is often applied to a wide range of circumstances. The International Labour Organization's (ILO) Working Conditions Laws Report includes working hours and annual leave, maternity protection, and minimum wages. Other literature interprets working conditions more broadly and includes compliance with national laws and international norms (often defined by ILO conventions). Labor practices that generate working conditions that fall short of these standards are often referred to as poor labor practices in both the literature and this report. In practice, factory-level compliance reports are often used to measure working conditions. This report uses a broad definition of working conditions and draws upon factory-level reports for examples and illustrations of broader points in the literature.

The organization of the review addresses six important points. The first section provides an overview of the literature that describes labor practices in developing countries generally and Asian apparel factories in particular. The main conclusion is that apparel factories have been widely criticized for having poor working conditions. The second section describes some of the determinants of poor practices that lead to the poor working conditions. This section shows that the determinants are complicated and subtle, but there are clear policy options to address the determinants. Some of the leading policy responses are described in the third section. The fourth section lays out criteria that might be used to identify "optimal" labor practices and identifies some of the obstacles that might keep countries from successfully implementing optimal policies. One of the obstacles is government enforcement, which is why the fifth section focuses on the extent to which the design of labor regulations should incorporate enforcement capacity. The main message of this section is that in developing countries, enforcement capacity is often quite limited due to limited resources. In response, it has been increasingly understood that successful approaches require cooperation from multiple stakeholders. The sixth and final section offers concluding thoughts and focuses especially on some of the approaches that seem to have been particularly successful in improving working conditions.

## II. LABOR PRACTICES IN FACTORIES IN ASIA

Labor practices in developing countries generally, and often in Asian factories in particular, are criticized widely for being “poor” or “unacceptable.” In 2005, the International Labor Organization reported that nearly 9.5 million people work in “slave-like conditions” in Asia (ILO 2005a). Often-cited examples of poor practices include wages below living wages, excessive hours and days worked per week, discrimination, verbal and physical abuse, suppression of trade unions, and preventable disasters that result in death.<sup>1</sup> Popular stories, such as the collapse in Bangladesh’s Rana Plaza, create the impression that labor practices are very poor.

Independent of popular perceptions, however, it is important to point out that Asia is extremely diverse: Japan and Bangladesh have very different labor practices. As described by Robertson et al. (2009), poor practices in developing country factories often are a reflection of development status. Practices in developing country factories are considered poor when compared to developed countries. Developing countries, by definition, are often characterized by low productivity, relatively low education levels, low wages, and volatile economic conditions. These conditions result in poor conditions generally (not just in factories) that include malnutrition, infant mortality, low education levels, and other poverty-related problems. Low wages, long hours, and unfavorable working conditions within factories, therefore, are often a reflection of development status.

Much of the difference in working conditions across countries is explained by differences in levels of development. To illustrate this point, consider one of the most salient and illustrative examples of such conditions: working hours.<sup>2</sup> Figure 1 shows the negative relationship between working hours and gross domestic product (GDP) per capita. The negative relationship is statistically significant and shows that poorer countries tend to work longer hours (often more than the 40-hour-per-week standard in many developing countries). South and Southeast Asian countries fall below the predicted line, but are not far from their predicted values.

Governments may enact progressive laws to improve conditions, but often, enforcement is expensive. The lack of resources generally may mean that enforcement is insufficient to maintain standards intended by the law (Amengual 2014a, 2014b, Lee and McCann 2014, Weil 2014). When government enforcement falls short, tension between public and private enforcement emerges and pressure on factories to improve their standards comes from other stakeholders (Weil 2005, Willborn 2014).

Another key concern about working hours is that poor countries may have progressive worker protections, such as established limits for weekly work, but actual hours worked may exceed these values. To illustrate this point, Figure 2 shows the ratio of actual hours worked to the legal established “normal” workweek. Values above 1, therefore, suggest a prevalence of overtime work (which may, of course, be legal) or workweeks longer than established norms. Again, the figure shows a negative relationship. The negative relationship highlights the fact that workers in developing countries work longer relative to their own domestic norms than richer countries. Again Asian countries fall close to

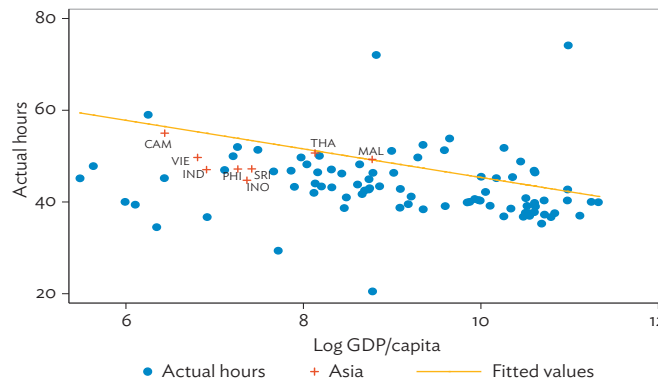
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<sup>1</sup> Criticisms found in the popular media include those of the Worker Rights Consortium (2013) and <http://www.workersrights.org/>, the European Center for Constitutional and Human Rights ([http://www.ecchr.eu/en/our\\_work/business-and-human-rights/working-conditions-in-south-asia.html](http://www.ecchr.eu/en/our_work/business-and-human-rights/working-conditions-in-south-asia.html)), and others. The ILO (2010a and 2015a) echoes these concerns when examining the wage and employment situation throughout the Asia and Pacific region.

<sup>2</sup> Robertson et al. (2009) demonstrate the same point with other measures of working conditions.

their predicted values. The People's Republic of China (PRC) is a notable exception in which workers work more hours per week than their established normal limit—far more than would be predicted by the PRC's GDP per capita.

**Figure 1: Working Hours and GDP per Capita**

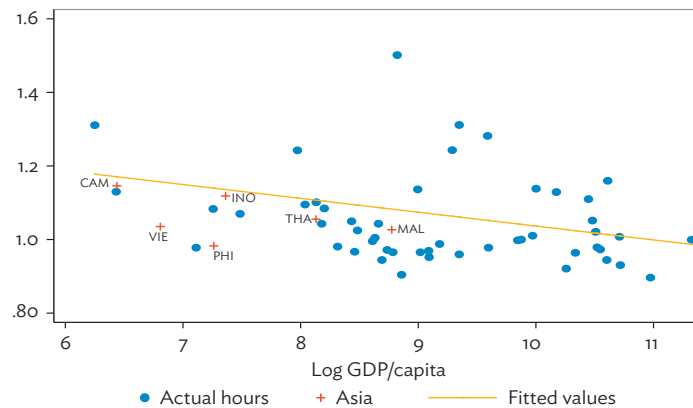


CAM = Cambodia, GDP = gross domestic product, IND = India, INO = Indonesia, MAL = Malaysia, PHI = Philippines, SRI = Sri Lanka, THA = Thailand, VIE = Viet Nam.

Notes: Working hours data are drawn from household surveys. The working hours are the usual hours per week for all workers and are the mean values over the 2005–2015 period in order to present long-run averages. GDP per capita data are from the World Bank Development Indicators and are the natural log of 2005 dollar valued GDP divided by population.

Source: Authors' elaboration using working hours data from the ILO database.

**Figure 2: Working Hours Relative to Regular Weekly Hours Limits**



CAM = Cambodia, GDP = gross domestic product, INO = Indonesia, MAL = Malaysia, PHI = Philippines, THA = Thailand, VIE = Viet Nam.

Notes: Working hours data are drawn from household surveys. The working hours are the usual hours per week for all workers and are the mean values over the 2005–2015 period in order to present long-run averages. GDP per capita data are the natural log of 2005 dollar valued GDP divided by population.

Sources: ILO database; World Development Indicators; ILO 2010b. *Working Conditions Laws Report 2010 A Global Review*. Geneva.

Other examples of poor conditions in factories in Asia are ubiquitous and have received a great deal of attention in the popular media (see Box 1). Formal analysis of these conditions, however, is not so common. Concerns about working conditions emerged in analysis about East Asia's Newly Industrialized Countries (NICs) as early as the 1980s (Addison and Demery 1988). When taking an academic view of these conditions, researchers often group these practices under the rubric of human resource policies, since they include wages, hours, environment, sanitation, and other dimensions that are set by factories. As a result of these practices, conditions in factories in developing countries are often called “sweatshops” and have a large and growing literature. This paper reviews several aspects of this literature with the goal of describing labor practices in factories in developing countries generally and in Asia in particular.

### Box 1: The Rana Plaza Collapse

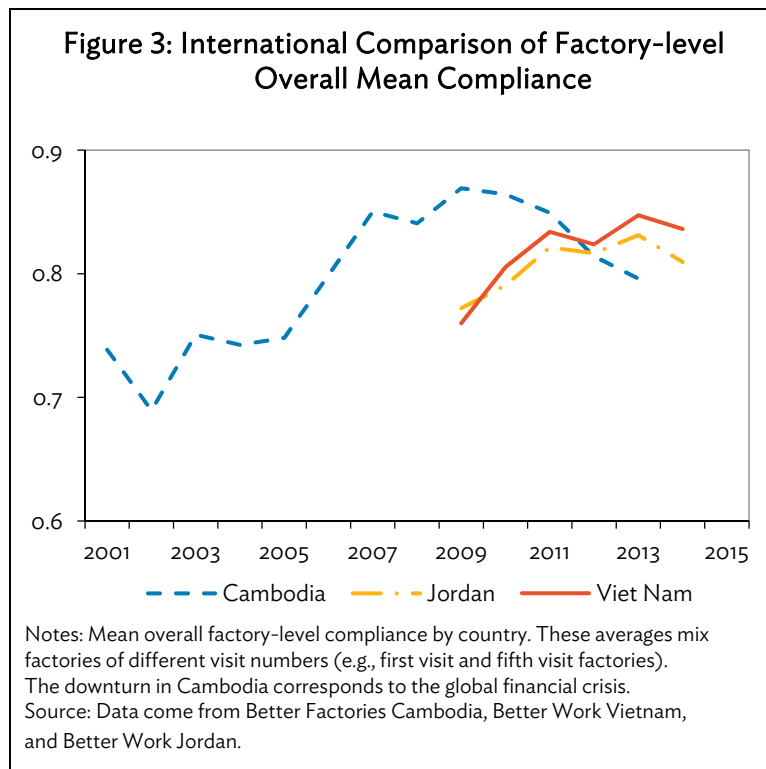
On 24 April 2013 more than 1,100 apparel workers died when a factory complex collapsed in Rana Plaza. Since that time, European and United States buyers have dedicated considerable efforts toward addressing safety concerns in Bangladesh. The Accord on Fire and Building Safety in Bangladesh (“The Accord”), the Alliance for Bangladesh Worker Safety (“The Alliance”), and the National Initiative were collections of apparel buyers (mainly from the United States and Europe) that now cover about 89% of the Bangladesh apparel workers (Anner and Bair 2016). These programs seek to help factories invest in safety improvements while mitigating the effects on factory competitiveness. Factory fires as recently as 1 February 2016 demonstrate that ongoing efforts are necessary to minimize safety risks in these apparel factories.

## A. The Apparel Sector

Just as factory practices vary with development status, so does the propensity to export apparel. Historically, apparel has been one of the first steps into manufacturing that countries take along the path to development (Fukunishi and Yamagata 2014). Garment exports from developing economies increased significantly after the Second World War and were led by Japan; the Republic of Korea; Hong Kong, China; and Taipei, China. As these economies became richer, their apparel production shifted toward lower-wage economies and apparel production has more recently been led by the PRC, Viet Nam, Cambodia, and Bangladesh.

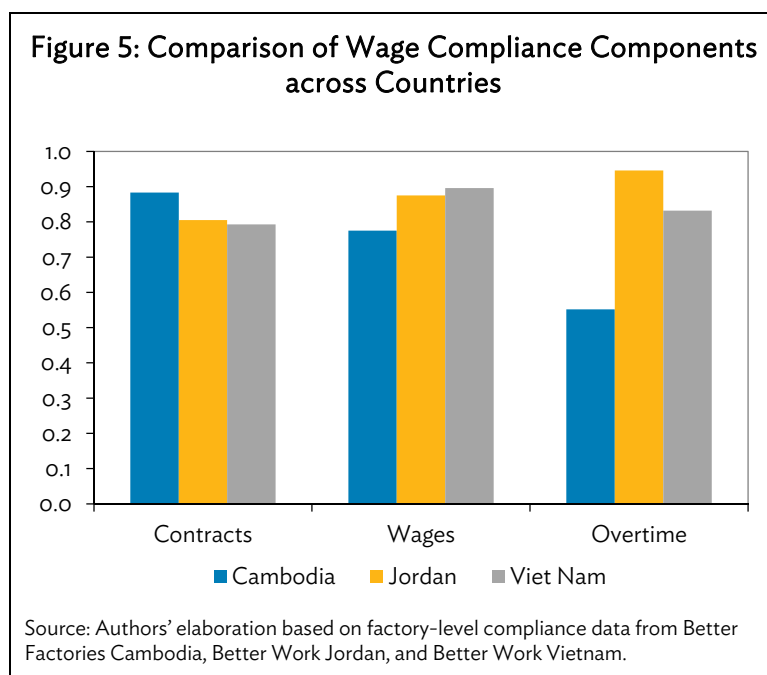
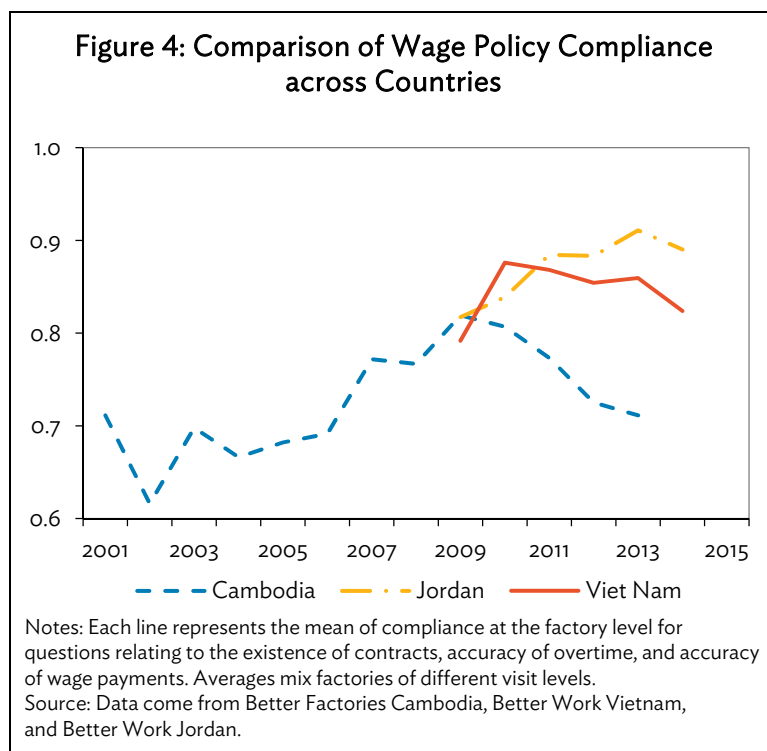
It is important to note that although there is a coincidence between development status, apparel production, and unfavorable labor practices, it would be inaccurate to conclude that working conditions are especially poor in the apparel sector. In fact, when compared to other sectors where apparel workers would be employed, the apparel sectors are often higher paying and safer. For example, Robertson et al. (2009) present five case studies that suggest that wages are higher and accidents are lower in the other sectors where the “typical” apparel worker would alternatively be employed (especially agriculture).

To illustrate some of the differences in compliance with national and international standards, Figure 3 shows the mean factory-level compliance levels for apparel factories participating in Better Work Jordan, Better Work Vietnam, and Better Factories Cambodia. Better Factories Cambodia started in 2001 and the other two started closer to the end of the same decade. Note that in all countries, mean factory-level compliance starts low, but compliance started lower in Cambodia. Information about compliance may have evolved over time. Note that in all three countries, compliance increases over time, but in Cambodia, compliance falls during the global financial crisis.



Overall, mean compliance may hide some of the variation across countries within certain categories. One of the main concerns is with wage policies: Are wages paid accurately and on time? Are wage rates clearly conveyed to the workers in contracts? Are overtime wages accurately paid? Figure 4 compares compliance in wage policies across countries and shows that compliance increases over time until the financial crisis of 2008 when wage pressures may have significantly increased for buyers and factories. Figure 5 shows that the underlying categories in wage policies have different levels of compliance across countries. To the extent that the compliance averages are comparable, Figure 5 shows that Cambodia has lower compliance in overtime than Viet Nam and Jordan, while Viet Nam and Jordan tend to have lower compliance in issues relating to labor contracts.

Many of the changes in compliance tend to be correlated. Brown, Dehejia, and Robertson (2015) undertake a factor analysis, which is an empirical technique designed to identify underlying correlations between various variables, and find that changes in compliance tend to fall into six main groups: communication, occupational safety, modern human resource practices, compensation, unions, and core labor standards. Improving some categories may facilitate changes in others later on. For example, Rossi and Robertson (2011) find that improvements in communication and relationships with supervisors often precede improvements in other areas, which suggests that improving communication may be an important step toward improvements in other areas.



Of course, the lack of comparable working conditions data from other sectors makes comparisons across sectors difficult. Nevertheless several studies, such as Robertson et al. (2009) suggest that conditions in apparel may be higher than in other sectors. One reason that conditions in apparel factories are better than other domestic alternatives might be that many apparel factories are globally engaged. The current structure of global apparel production is characterized by vertically integrated *value chains* that include buyers (such as Gap, H&M, Levi's, and other brands) and factories

that produce for these buyers but are generally not owned by the buyers. Some argue that such disaggregation puts compliance issues at arm's length from the buyers while gaining a cost advantage from lower labor costs (Glynn 2011). The conventional wisdom is that buyers seek out the lowest production costs. Several authors point to specific examples where low wages are an important determinant of increases in exports in Bangladesh (Yunus and Yamagata 2014), Viet Nam (Goto 2014), and Madagascar (Fukunishi and Ramiarison 2014). In particular, Goto (2014) suggests that wages in Viet Nam were slow to rise while exports were rising, which may have contributed to the sustained growth of the industry.

While wages are important, buyers make purchasing decisions based on a range of factors, including global trade policy. One of the most recent global trade policy shocks to the apparel sector was the end of the MFA at the end of 2004 (Lopez-Acevedo and Robertson 2012). The end of the MFA resulted in significant reallocation of global apparel production, with a particular shift away from Latin America (especially Central America and the Caribbean) toward East Asia generally and the PRC in particular (Frederick and Staritz 2012). When compared across countries, however, low wages do not always emerge as the driving factor. Fukunishi (2014) compares Bangladesh, Madagascar, and Cambodia and suggests that human capital and productivity growth can sustain higher wages while increasing exports. In a multicountry regression analysis, only about one-third of the change in apparel production was explained by low wages (Lopez-Acevedo and Robertson 2012).

The rest was explained by a range of other factors that producers and buyers take into account, such as past experience, access to materials, utilities (electricity and water), infrastructure (roads and ports), and (good) working conditions. For example, Mostafa and Klepper (2009) suggest that Bangladesh was able to build on a strong history of garments in order to build its export market. While it might be tempting to equate poor conditions with lower costs, and therefore suggest that buyers seek out poor conditions, several authors have suggested that buyers do not necessarily seek out the lowest working conditions *per se* (see Box 2). Asuyama and Neou (2014), Brown, Dehejia, and Robertson (2014a), and Beresford (2009) show that Cambodia has increased working conditions and exports at the same time. Yunus and Yamagata (2014) also imply that attempts to comply with labor standards contributed to the growth in apparel exports in Bangladesh.

### Box 2: Global Engagement and Working Conditions

While some suggest that engaging with the global economy leads to a race to the bottom in working conditions, Kucera (2002) finds that multinational corporations (MNCs) tend to be attracted to countries with stronger worker rights. The countries with the lowest standards generally have very poor institutions, which makes them unattractive for foreign investment. While MNCs do enter environments where the wages and working conditions are already below the standards in developed countries, it is not clear that MNCs make conditions worse. Several empirical studies find that MNCs and foreign direct investment are associated with higher employment, higher wages, and better working conditions over time. Global Exposure increases the demand for labor: firms have more economic opportunity through exports and the expansion of exports creates jobs that were not present. Several studies demonstrate job gains from global engagement, such as Kabeer and Mahmud (2004) in Bangladesh; Nadvi et al. (2004) in Viet Nam; Humphrey, McCulloch, and Ota (2004) in Kenya.

The garment industry faces many significant challenges in developing countries. In India, for example, the sector is dominated by smaller firms that may be less able to implement modern production techniques (Hasan et al. 2017). Challenges like these take on particular importance because in most countries most of the apparel workers are women. Allegations of harassment and sexual abuse are not uncommon. Women are also more likely to report emotional stress in garment

factories. Women face unique challenges in starting businesses and formalizing their businesses (Babbitt, Brown, and Mazaheri 2015). In the few countries where the majority are not women, such as in Pakistan, firms are striving to hire more women and firms that have hired more women have higher survival rates (Makino 2014).

## **B. Formal and Informal Firms**

When talking about the differences between formal and informal firms, the first issue that comes up is the definition of formality. Differences in studies of “formality” in the academic literature often depend on definitions of formality. Paying taxes, participating in the national social security system, and providing formal benefits are three of the main criteria often used to delineate formality from informality. The conventional wisdom is that informal sector employment is “worse” because wages are lower and workers are not covered by government protections. As a result, the informal sector is usually seen as a problem and a sign of underdevelopment that serves as an inferior alternative to formal sector work.

The academic literature, however, suggests that the picture of the informal sector is not quite that simple. There are two main debates surrounding informality in the academic literature. The first is whether or not formality is optimal for workers. The argument for the optimality of informality often raises issues of flexibility and control, but also at times relates to wages. Both Maloney (2004) and Staneva and Arabsheibani (2014) find that workers in the informal sector earn higher wages than their comparable counterparts in the formal sector in Latin American and Tajikistan. Similarly, Harrison and Scorse (2010) report that wages in Indonesian textile, apparel, and footwear firms supplying the export market were actually lower than those supplying domestic markets prior to the antisweatshop agitation of the mid-1990s. The gap, however, reversed following a period of attention by international buyers concerned with the reputational externalities generated by their vendors.

This is often seen as a surprising result because it goes against the conventional wisdom and may not apply to South Asia. It has been shown in many studies that larger, formal-sector, exporting firms pay higher wages. One reason for the discrepancy might be that the wage premiums paid by the (larger) foreign-oriented firms are often offset by longer work hours (Fukase 2014). The conventional perception that workers in the informal sector are necessarily worse off may often be true, but cannot be taken for granted.

One of the lessons presented by the differences between the formal and informal sectors is that these differences give rise to sorting among working populations. McCaig and Pavcnik (2015) and Babbitt, Brown, and Mazaheri (2015) suggest that among women, the preferences for formal sector work are heterogeneous. Younger workers are more likely to choose formal sector work if given the choice. McCaig and Pavcnik (2015) find that less-educated, older, rural workers have less opportunity to join the formal sector, which is consistent with the conventional wisdom that informal sector work is often the alternative for workers who cannot find formal employment. Informal sector workers who earn more are often entrepreneurs or workers who value the flexibility informality provides. In other words, selection issues are very important when discussing the differences between formal and informal sectors.

For production workers, however, like most apparel workers, it is not clear that informality would pay more. Informal sector workers do not have the protection, even if limited, that the law would provide for working hours and pay rates. One of the ways this protection is particularly important is through the use of short-term contracts, which in many ways are in the grey area between formality and informality



(ILO 2015b discusses the employment insecurity that is partially driven by the increased use of short-term and part-time contracts). Short-term contracts are in many cases legal alternatives to long-term contracts, but they allow producers to avoid providing protection and benefits that long-term workers receive. In many cases, the government puts limits on the amount of time short-term contracts may be applied to particular workers, but anecdotal examples of employers circumventing these limits are common.

One way that employers have been able to circumvent limits on short-term contracts is by subcontracting. Subcontracting by exporting firms often generates linkages between formal sector exporters and much smaller informal sector producers. For the apparel sector in particular, however, the linkages between formal and informal sector firms are very important. Formal-sector exporters often will subcontract to informal sector firms during times of peak demand. Subcontracting to informal sector firms poses particular problems for regulators and stakeholders because the subcontracted firms, by definition, are not held to the same standards that the formal sector contracted firms are expected to uphold. For example, formal contracted firms may be audited by the buyers or their representatives, but the subcontracted firms rarely are. Mukim (2015) describes some of the complicated relationships between the formal and informal sector firms in India and suggests that there may be benefits to both the contracted and subcontracted firms from these relationships. Basole, Basu, and Bhattacharya (2015) find similar results, and also conclude that the relationship between the formal and informal firms are complex. For example, subcontracting can benefit smaller and more remote firms through technology transfer, but can hurt larger, urban firms.

### III. DETERMINANTS OF POOR PRACTICES

The distinction between formal and informal does not take us far enough in understanding why some firms decide to implement poor practices. Certainly, poor conditions in the informal sector may be, by definition, the result of operating outside the law. But many of the concerns about poor practices are directed at the larger, formal sector factories. The fact that poor practices are found in both informal and formal factories implies that the law is one of possibly several determinants of poor practices.

Different academic disciplines take different approaches to understanding the behavior of firms. Economists often assume that factory managers are making decisions with the goal of optimizing some objective, which is usually maximizing profits. As noted earlier, decisions about working conditions are a subset of the decisions factories make and these decisions can be grouped generally under the rubric of *human resource management* (HRM) policies. These policies intersect with national and international labor standards, but also are driven by the economics of the factory itself.

The literature related to HRM policies spans more than 50 years (McGregor 1960 is one of the earlier examples). Much of the debate in the HRM literature focuses on the issue of incentives. Unlike machines, workers make their own decisions that affect their performance at work (e.g., effort). Worker motivation and work quality are influenced by job characteristics (Hackman and Oldham 1976). HRM policies therefore can have both direct and indirect effects on costs. For example, putting in air-conditioning includes a direct cost of the air-conditioning unit. The indirect cost effects arise with the change in worker productivity that may result from climate control. Huselid (1995); and Ichniowski, Shaw, and Prennushi (1997) are two early studies in the new wave of academic literature that document increases in worker productivity after implementing new HRM policies. Shaw (2004) attributes the growth in United States (US) productivity in the 1990s to HRM policies (although

acknowledging measurement problems), and Lazear and Shaw (2011) describe how firms can optimally design their HRM policies to increase productivity by describing specific policies that have been linked to productivity growth.

One particular area of HRM policies that have been linked to productivity is relationships with supervisors. Leblebici (2012) reports that 100% of sampled workers agree that their productivity is affected by their relationships with their supervisors. As mentioned earlier, Rossi and Robertson (2011) find that improving communication between supervisors and employees can pave the way for subsequent HRM innovations. While these results raise the question of the direction of causality (Wright et al. 2005), both literature reviews (Bloom and Van Reenen 2011 and Croucher et al. 2013) and meta-analyses (Judge et al. 2001 and Combs et al. 2006) find that the preponderance of the literature points to a causal relationship that runs from the relationships to worker productivity.

In addition to relationships with supervisors, other specific aspects of working conditions have been found to be significantly related to worker productivity, including incentive pay (Jones, Kalmi, and Kauhanen 2010 and Lazear and Shaw 2011) and training (Singh 2004). Improvements in productivity may require that workers are well educated (Shaw 2004) or that the changes are implemented in a way that makes them understood by workers (Black and Lynch 2001), but the gains apply to a range of workers within plants (Jones, Kalmi, and Kauhanen 2006). Brown, Dehejia, and Robertson (2013 and 2014b) find that there is evidence of a positive relationship between firm compliance with labor standards and firm survival and that firms that try innovations in HRM policies, such as compliance, are not very likely to reverse those decisions. The main point from these studies is that improvements in HRM policies can improve worker performance and perhaps firm performance as well.

Improved working conditions are also correlated with increased productivity and firm profits. Brown et al. (2015), analyzing firm-level data from Viet Nam, find that compliant firms are more profitable. Further, profits increase as firms become newly compliant. The price-cost ratio nearly doubles over five Better Work assessment cycles. Evidence on a causal relationship is provided by Levine, Toffel, and Johnson (2012). Analysis of random OSH inspections of California firms found that inspected firms subsequently experienced significant reductions in costs associated with accidents and injuries with no reduction in the size of the workforce.

The main question that follows from this growing and important literature, of course, is why factories would resist implementing improvements in HRM policies if they have been shown to increase worker and factory performance. In other words, what explains the choice of poor practices at the firm level and the persistence of poor practices in developing countries?

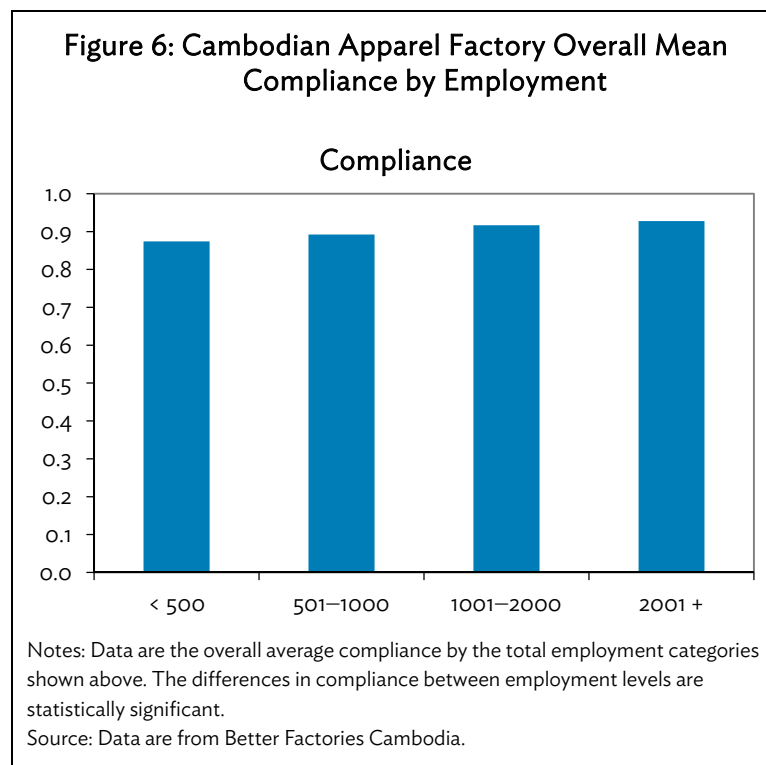
There are several leading explanations in the literature. The first is that the economists' assumption of perfect information may not hold in developing countries. It is fairly well-known that developing countries do not usually use the most recent or "cutting edge" production techniques. Alvarez and Robertson (2004), for example, show that Mexican and Chilean firms are most likely to use older production technologies. Since more innovation takes place in developed countries, it takes some time for new techniques to spread to the rest of the world.

If we view HRM policies as a form of technology, and it seems reasonable to take that view (Shaw 2004), then it is possible, and probably likely, that developing country firms may not be aware of the alternative policies. The fact that Lazear and Shaw (2011) describe specific HRM policies that firms can implement to improve productivity suggests that there are factories in developed and

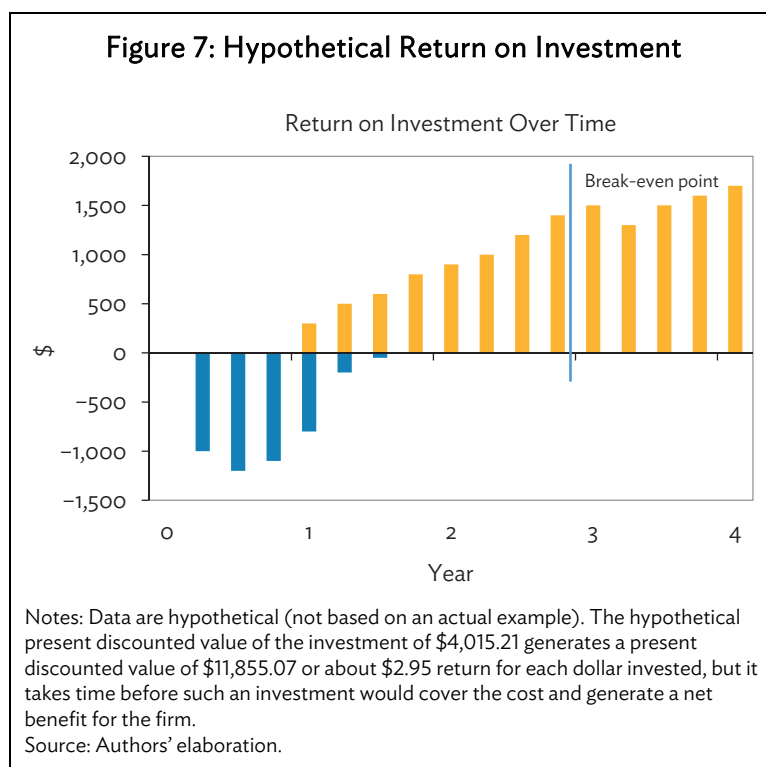
developing countries that may not yet be aware of these HRM policies.

Even if factories are aware of the alternatives, they may not be aware of the positive results that might follow from such changes. The role of information has been shown to be especially salient for developing country producers. In particular, Bloom et al. (2013) find that firms benefit from new information. Using a randomized experiment of consulting services in India, they show that firms that received the new information in the form of consulting services increased their performance. In developing countries, the issue of information may be especially relevant because firms tend to be smaller (de Grip and Sieben 2005).

Even if factories are aware of the technology and aware of the net benefits, they may not be large enough or have a sufficiently long expected time horizon to capture the expected benefits. Size matters because the up-front costs may be fixed and production volumes are not sufficient to lower the average cost to make the investment pay off. Figure 6 shows that larger firms are more compliant, which is consistent with the idea that fixed costs matter.



The idea of cost-benefit analysis helps illustrate the importance of a longer expected time horizon. The concept of return on investment is well-known. Up-front costs are made with the expectation of capturing long-run gains. Comparing the present discounted value of the costs and benefits of such investments generates a return on investment metric that helps evaluate the benefits of the project. In Figure 7, the hypothetical present discounted value of the investment of \$4,015.21 generates a present discounted value of \$11,855.07, or about \$2.95 return for each dollar invested. Factories in developing countries, especially in apparel, are smaller, often newer, and are more likely to close. As a result, factory managers may not know what the relevant time horizon is for their factory and therefore be reluctant to make investments that take time to pay off.



Another leading explanation is that the innovations in HRM policies require that both workers and managers understand the policies and understand what aspects would affect worker motivation (Khilji and Wang 2006, Bowen and Ostroff 2004). It takes time and resources for managers to know what workers value, and therefore managers may not have a good understanding of what motivates workers (Domat et al. 2013). Employee perceptions of support from managers seem to matter a great deal (Kuvaas, Dysvik, and Buch 2014). Employee trust of supervisors is one key aspect of this support. In particular, Helliwell and Huang (2005 and 2007) and Helliwell, Huang, and Putnam (2009) show that firms do not fully appreciate the value that workers place on trust and workplace social capital. Improving trust within the workplace can have at least as much of an effect on worker life satisfaction as an increase in income. In a similar vein, Herzog and Schlottmann (1990) find workers would give up wages to increase workplace safety. Firms that operate on the edge of profitability, like many developing country apparel firms, may not understand the long-run benefit of a short-run investment in time or resources necessary to make the HRM policy changes.

A third reason is that firms may simply follow local norms rather than do an independent cost-benefit analysis of different policies. Brown, Dehejia, and Robertson (2015) apply a model of norm formation to explain the decision to become compliant with global labor standards in Cambodia. Their results suggest that local norms are important for firm decisions, but experimentation and learning are also significant, which suggests that both norms and learning (that is, new information) are important explanations as to why firms choose poor practices. The implication is a powerful one in the sense that sharing information, and finding ways to generate incentives for experimentation in HRM policies might be effective ways to improve working conditions in developing countries.

A fourth reason is that firms may find abuse techniques are profit maximizing in some situations. Rubin et al. (2015) analyze the decisions related to wages and hours. Increased work hours

are optimal if orders are uncertain. International buyers who do not place orders with factories with sufficient lead time for production planning have the effect of producing an optimal workday of variable length. In such a situation, firms will find it optimal to accept all orders and set the workday sufficiently long to complete all accepted work. Firms must then employ a set of strategies to induce workers to accept the length of the workday optimal for the firm. The first best strategy is to pay a very base pay so that workers will require overtime in order to remain employed. If workers also experience cognitive dissonance and the optimal work day is extremely long, firms will employ a strategy of forced overtime that may involve techniques such as locking doors or verbally abusing workers who refuse overtime. Absent the ability to force overtime or pay extremely low base pay, firms will employ a dismissal threat strategy. Workers are offered extremely short contracts (2 months), which are renewed conditional on accepting overtime.

A fifth reason concerns the processing of information linking working conditions and firm performance. Hanna, Mullainathan, and Schwartzstein (2014) note that managerial attention is a scarce resource within an organization. Firm managers must choose which dimensions of production to devote managerial attention. In an experiment with Indonesian seaweed farmers, Hanna, Mullainathan, and Schwartzstein (2014) found that firms randomly assigned to various pod sizes did not process information related to optimal pod size. The effect of pod size on productivity was internalized only after seaweed farmers were presented with summary data identifying the optimal pod size.

#### IV. DIFFERENT APPROACHES USED TO IMPROVE PRACTICES

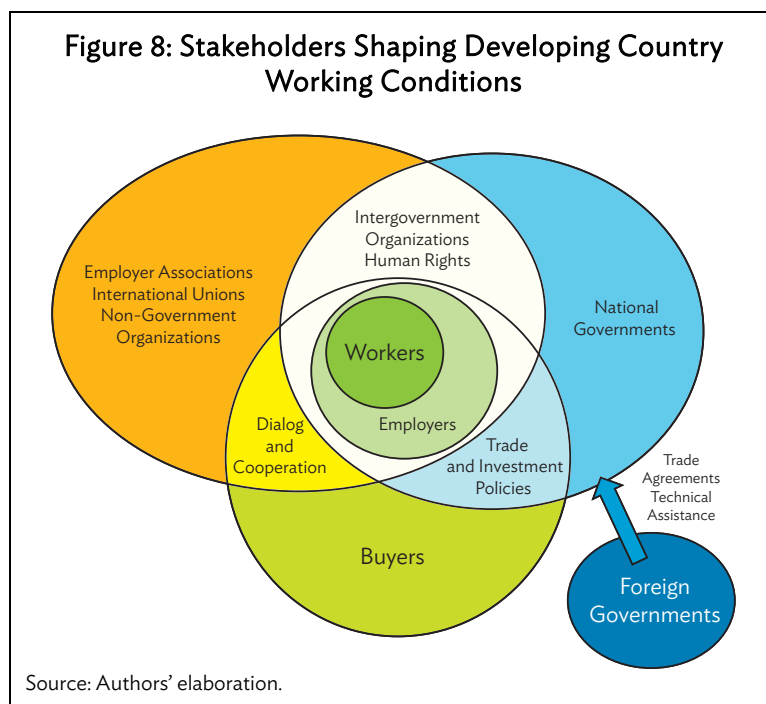
Improving practices is a goal that is shared by many stakeholders. A useful framework for describing the different approaches used to improve practices is based on identifying the relevant stakeholders and the roles they play. Figure 8 presents a Venn-like diagram of the different stakeholders that either have taken unique approaches or have been very influential in shaping the approaches others have taken. Figure 8 highlights the fact that different approaches to improve practices do not occur in a vacuum. In fact, collaborative governance is becoming more important and possibly more commonly found in successful cases (Gereffi and Mayer 2004, Miller et al. 2009, Barrientos et al. 2011, Gereffi and Lee 2016, Mayer and Pickles 2014, and Oka 2014).

At the center of Figure 8 are the workers, who are most directly affected by the different approaches to improve working conditions. The next circle out includes the employers, whose particular approaches are often assumed to be guided by optimizing behavior and are discussed above. The next set of actors includes national governments, buyers, and other organizations, such as employer organizations, international unions, and nongovernment organizations (NGOs). On the periphery are foreign governments. Each of these approaches are discussed in turn below.

Workers, at the center, are often represented by unions. Miller et al. (2009) suggest that employers continue to resist collective bargaining. Unions focus on organizing workers promoting freedom of association and collective bargaining. Unions provide ways to resolve workplace disputes and offer protections to workers that can include improvements in workplace conditions (Freeman and Medoff 1984). By working with international unions, local unions can increase their leverage and negotiate with employers and employer organizations.<sup>3</sup>

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<sup>3</sup> The recent agreement in the textile sector in Jordan is one such example. See (<http://www.industrialunion.org/textile-workers-reach-sectoral-agreement-in-jordan>).



Buyers, as representative of transnational corporations and their organizations, have also taken several approaches to improve working conditions. In the 15 years, these approaches have become more common and extensive. OECD (2002) reported that only 20% of global companies had policies that applied to their suppliers. Today, most, if not all, corporations have developed codes that apply at least in part to their supply chain. These codes fall under the rubric of Corporate Social Responsibility (CSR). CSR initiatives are becoming increasingly common, which may indicate that CSR programs have positive effects on firms. Erhemjamts, Li, and Venkateswaran (2013) investigate the impact of CSR on firms' performance. They find that the firms with good characteristics, such as better performance, higher research and development intensity, better financial health, and operating in new economy industries are more willing to engage in CSR measures. Further, stronger CSR is always associated with better investment policy and organizational strategy. Servaes and Tamayo (2013) also find that CSR activities, as a signal of high public awareness, can increase the value of the firms. Locke and Romis (2010) provide some case study evidence from Mexico suggesting that HRM innovations may benefit firms. Of course, establishing the direction of causality remains elusive; it may be that more productive and successful firms are more likely to be able to afford CSR activities. More research, therefore, is necessary.

While some studies have described positive effects of CSR initiatives and corporate codes of conduct, these codes are often criticized. One of the leading reasons these codes are criticized is that corporate incentives may conflict. Seeking to maximize profits by minimizing costs while at the same time seeking to maximize profits through developing a strong reputation for ethical sourcing may not always be consistent, especially in the short run (Hoang and Jones 2012). Oka (2010a, b) and Ang et al. (2012) show that reputation matters; reputation-sensitive buyers are generally associated with developing country producers that are more compliant with national and international standards. Furthermore, the common practice of outsourcing in apparel generates supply chains that can result in production of at least some stages being far removed from the corporate buyers.

National governments have tremendous potential to affect working conditions, and the approaches national governments take are usually linked to domestic laws.<sup>4</sup> Together these laws establish the national labor policies and institutions (Lee et al. 2014) that shape “the behaviors of firms and the conditions of work and employment” (p.88). Main labor institutions’ concerns in recent years are minimum wages, working time, collective bargaining, and employment protection. The study of labor institutions is necessary because effective institutions are a key factor in economic development. Challenges still exist in countries with massive informal employment, however, as discussed earlier.

One of the leading examples of national government policies is the minimum wage. In some countries, like Cambodia, the minimum wage only applies to the apparel sector. Developed countries, such as the United Kingdom (1999), Ireland (2000), and Austria (2009), have introduced a national minimum wage during the past 10 years or so. Developing countries also increasingly rely on minimum wages. Currently, about 90% of countries have applied minimum wages (ILO 2010a).

To many, the idea and effect of the minimum wage is very straightforward. Increasing the wage floor guarantees a minimum standard of living for the working poor. Grimshaw, Bosch, and Rubery (2014) mention some other goals relevant to minimum wage policy that may be emphasized by unions, employers, or government, such as “increased labor market participation, controlled wage growth, improved social dialogue, reduced informal employment, higher income tax revenues and lower welfare and in-work tax benefits”(p.126). In the academic literature, however, the effects of the minimum wage in developing countries are hotly debated. The standard economic model predicts that employers will hire fewer workers at the higher wages (that is, the labor demand curve slopes downward). This prediction is not always supported in empirical studies. For example, Groisman (2014) analyzes the minimum wage policy in Argentina and finds that the formal employment is not reduced and informal employment is not increased because of the policy. The impact of minimum wage policy plays an important role in wage determination in both formal and informal employment.

Dozens of NGOs work to improve working conditions. Some of the leading organizations are shown in the following table. Many of these appear in academic literature and in the popular media. O’Rourke (2006) evaluates the nongovernmental labor regulation initiatives in the US and Europe. In the popular media, Resnikoff 2014 describes how the work of The Worker Rights Consortium (WRC) in the Dominican Republic seems to suggest that higher wages and improved working conditions are not barriers to successful apparel production. There are many other well-focused programs that address specific aspects of unacceptable forms of work in developing countries.<sup>5</sup> Through the empirical analysis of Worldwide Responsible Apparel Production (WARP), Social Accountability International (SA8000), Fair Labor Association (FLA), Ethical Trading Initiative (ETI), Fair Wear Foundation (FWF), and Worker Rights Consortium (WRC), and their participation in global governance, the results suggest that NGOs are helpful in improving the regulatory system and motivating the advance of global supply chains. NGOs not only benefit workers, but also bring the factory with successful, participatory, and local accountable improvements.

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<sup>4</sup> Examples of descriptions of these domestic laws are Lee and Svanberg (2013) for Viet Nam, Greenhouse and Harris (2014) for Bangladesh, and ILO 2005b for Cambodia.

<sup>5</sup> Fudge and McCann (2015) provide background for the ILO’s eighth Area of Critical Importance (ACI8): “Protecting workers from unacceptable forms of work.” The ILO identified these areas of critical importance in 2014–2015.

## Some Leading Organizations Working to Improve Labor Practices in Global Supply Chains

Organization	Brief Description
Clean Clothes Campaign	The Clean Clothes Campaign (CCC) works to expand and establish basic labor rights for workers in the global garment and sportswear industries. The CCC was founded in 1989, and is now allied with 16 different European Countries and over 200 organizations and unions.
Electronic Industry Citizenship Coalition	The Electronic Industry Citizenship Coalition (EICC) was founded in 2004 by a group of leading electronic companies involved in the global electronics supply chain. More than 100 companies are members of the EICC, which directly employs 5.5 million people and has an annual revenue of \$2.6 trillion.
Fair Labor Association	The Fair Labor Association (FLA) works with universities, civil society organizations, and companies to protect the rights of workers in a wide range of supply chains. The FLA conducts its own external assessments.
Fair Trade USA	Fair Trade USA is a third-party organization that certifies products by working with US companies and international suppliers. Fair Trade Certification implies living wages and a safe work environment.
Global Social Compliance Programme	The Global Social Compliance Programme (GSCP) was founded in 2006 to provide consistent compliance codes across supply chains and address the root issues surrounding noncompliance. The GSCP is currently comprised of 39 companies and actively engages civil society stakeholders in its programs.
Good Electronics	Good Electronics works to preserve and protect labor rights in the electronics supply chain. The Common Demands on the Electronics Industry, formulated by the Good Electronics network, addresses human rights issues not only within production plants but throughout the production cycle.
Labour Behind the Label	Labour Behind the Label is the UK platform of the Clean Clothes Campaign. Labour Behind the Label engages with trade unions and their local branches, consumer organizations, campaign groups, and charities to bring about meaningful and positive change in the garment industry.
Love Fashion Hate Sweatshops (War on Want)	The Love Fashion Hate Sweatshops campaign was started by War on Want, an organization committed to the fight against global poverty, inequality, and injustice. The UK-centered organization works with grassroots organizations around the world.
SweatFree Communities	SweatFree Communities is a campaign of the International Labor Rights Forum. Numerous cities, economies, and school districts have adopted “sweatfree” policies, outlined by SweatFree Communities.
The Institute for Global Labour and Human Rights (formally National Labor Committee)	The Institute for Global Labour and Human Rights (the Institute) is a nonprofit 501(c)(3) human rights organization that was founded in 1981 as the National Labor Committee. It produces research, in-depth reports, and public campaigns.

*continued on next page*



*Table continued*

Organization	Brief Description
Worker Rights Consortium	The Worker Rights Consortium (WRC) is an independent labor monitoring organization. The WRC also conducts research and has the support of over 175 college and university affiliates. The program started with a focus on the production and consumption of college and university-related apparel.
Worldwide Responsible Accredited Production	Worldwide Responsible Accredited Production (WRAP) works to make the production of goods in the sewn products sector safe, humane, and sustainable. WRAP has 1,725 certified factories, which employ over 1.5 million people.

Source: Authors' compilation from these websites, <https://cleanclothes.org/>, <http://www.eiccoalition.org/>, <http://www.fairlabor.org/>, <http://fairtradeusa.org/>, <http://www.theconsumergoodsforum.com>, <http://goodelectronics.org/>, <http://labourbehindthelabel.org/>, <http://www.warowant.org>, [http://www.sweatfree.org/about\\_us](http://www.sweatfree.org/about_us), <http://www.globallabourrights.org/>, <http://www.workersrights.org/>, and <http://www.wrapcompliance.org/>.

Some NGOs have taken the “social label” approach. Social labels are a form of certification program that attaches a physical label (in many cases) to a product whose production meets some minimum standards. According to Bair, Miller, and Dickson (2013), the “social label” approach can create a more ethical environment of apparel production. Social labels are able to convince the buyer, including individual consumer, a retailer, or a local government, that products meet certain minimum standards. Generally, social labeling reflects the antisweatshop movement, promotes ethical production and social-compliance industry, and thus becomes an effective approach to protect garment workers' welfare and improve labor practices. Social labels can be domestic or international initiatives. Some social labels discussed in the volume include, focusing on apparel production, “Sweat-free Communities” in the US (Ross 2013), “Garments without Guilt” in Sri Lanka (Goger 2013), “Better Factories” in Cambodia (Brown, Dhejia, and Robertson 2013), “Better Work” initiated by the ILO and International Finance Corporation, and so on.

Specifically, Goger (2013) examined Garments Without Guilt (GWG), a homegrown social labeling initiative developed by Sri Lankan companies supplying both Western business partners. This program was intended to address the observed immorality of apparel industry employment in urban-based, export-oriented enterprises. GWG focuses on issues such as free of child labor, forced labor, discrimination, and sweatshop practices while promoting women's empowerment and education. Particularly, GWG also deals with immoral working behaviors among women workers that conflict with Muslim ideals. The program was in the initial stage, and thus profound social outcomes have yet to be observed. Goger analyzes the challenges of GWG; for instance, GWG supplies start to question whether their buyers have sufficiently valued their efforts. Additionally, GWG lack an emphasis on freedom of association, collective bargaining, and living wages. Therefore, Goger concludes that “the process of becoming more ‘ethical’ is long, unstable, costly and fraught with risks” (p.64). In contrast, Brown, Dehejia, and Robertson (2013) found that Better Factories Cambodia, a model project of ILO's global Better Work initiative, had been successful in improving labor practices in Cambodia's garment sector.

At the intersection of national governments, NGOs, employer associations, and international unions lies the intergovernment organizations, such as the ILO. The ILO strives to improve working conditions worldwide and is the primary reference point for international labor standards. The work of the ILO is very well-known and the contributions of the ILO in this field are too numerous to be summarized here. For recent examples, readers might refer to reports by the ILO, such as ILO Director General (2011).

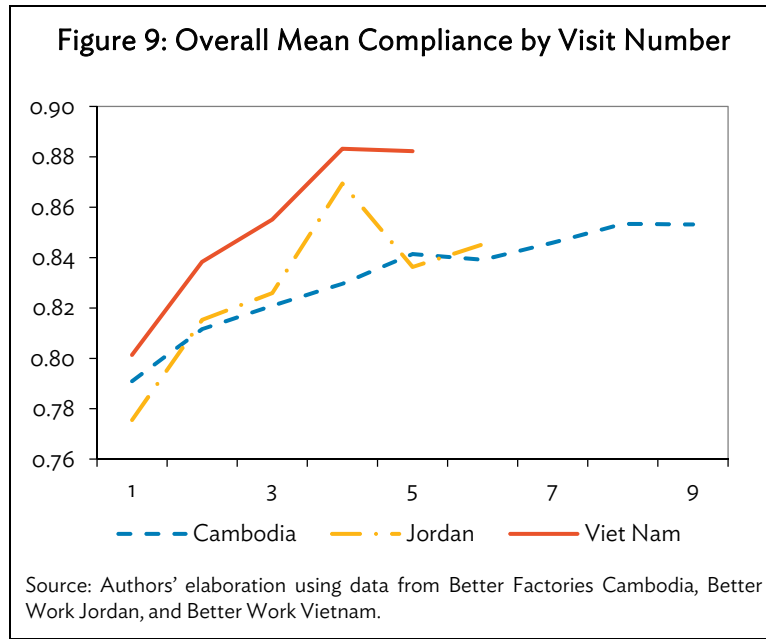
Foreign governments take different approaches. One approach is to coordinate labor laws within a multilateral system, as the European Parliament proposed in 1983 and 1994 and the US government proposed in 1986. In addition, every Ministerial meeting of the World Trade Organization between 1996 and 2001 considered such proposals (Brown, Deardorff, and Stern 2011). Nevertheless, these attempts have not succeeded. As an alternative, countries have increasingly incorporated labor standards into trade agreements.

Incorporating labor standards into trade agreements has raised significant controversy. Developing countries resist such provisions because they argue that they increase costs. Academics in developed countries have argued that there are more effective ways to address labor issues than trade agreements (Maskus 1997), but others are more optimistic (e.g., Elliott 2007). If labor standards in trade agreements raise costs, then we should be able to see these effects emerge in empirical studies. The empirical results, however, are mixed, especially in the areas of labor standards on factory performance (Bakhshi 2010, Kucera and Sarna 2006, Dehejia and Samy 2004, Bonnal 2010). Some find no effects on labor costs (Flanagan 2003), while others suggest that the provisions gave firms incentives to change production techniques in ways that improved conditions and performance (Huberman 2012).

A second approach is to require buyers to maintain standards throughout their supply chains. This approach has been especially salient in Europe. Following the development of the United Nations Guiding Principles on Business and Human Rights (also known as the Ruggie Principles) European governments have been developing National Action Plans that affect European producers. Across the Atlantic, both the US Department of State and the US Department of Labor have divisions that deal with international labor conditions.

A third approach foreign governments take is through technical assistance. The US Department of Labor supports projects that help foreign governments improve their enforcement and training capacity. Prominent examples include the “Vietnam Labor Law Implementation Project” (Industrial Relations Project, Phase II), which provides up to \$3 million dollars to help Viet Nam’s MOLISA, General Confederation of Unions (VGCL), and the Chamber of Commerce and Industries (VCCI) bring labor legislation in line with international labor standards.

The Better Work program brings together many of these stakeholders to help apparel factories identify and address a range of working conditions. This program has been broadly viewed as successful. For example, Figure 9 shows the changes in compliance in Jordan, Viet Nam, and Cambodia for apparel factories participating in the Better Work (or Better Factories Cambodia) program. The compliance with national and international standards, on average, increases with the number of Better Work factory visits. Figure 9 also shows that the pattern of compliance is similar across these different countries: rapid initial increases followed by slowing increases in compliance over time. This pattern may be explained by the factories addressing the “easiest” issues first (the “low hanging fruit”) and then addressing the more difficult problems later.



## V. WHAT SET OF LABOR REGULATIONS WOULD BE 'OPTIMAL'?

Economists base much analysis on the premise that agents seek optimality. The two relevant agents in this case are the firms and workers. The key to this approach is to understand what the firms and workers are optimizing.

For firms, the usual assumption is that firms maximize profits, either through maximizing revenue or minimizing costs. Some advocates, such as Powell and Skarbek (2006) argue that sweatshop conditions are optimal for firms. Sweatshop conditions reflect the profit-maximizing decisions of firms given their current information and constraints. Some evidence supporting this view can be found in the Harrison and Scorse (2010) study that found that international pressure to improve working conditions causes Indonesian firms to earn lower profits and ultimately relocate. The main implication of this view is that labor regulations that cause firms to deviate from their choices would be less optimal for firms. In other words, outside regulations would not be optimal for firms.

Of course, earlier in this paper, we present evidence that suggests that regulations do not necessarily make firms worse off. If regulation encourages experimentation that would not otherwise take place, then the regulation that imposes short-term experimentation and adjustment costs could induce learning (Fung, O'Rourke, and Sabel 2001; Bloom et al. 2013; Domat et al. 2013). In particular, the experimentation could cause firms to learn about alternative HRM policies that in the medium and longer term increase profits through improvements in firm performance. There are some examples of regulation having this effect. For example, Levine, Toffel, and Johnson (2012) describe a natural experiment in which random inspections by the US Office of Safety and Health Administration reduced costs from worker injuries by an average of \$350,000 per company. Asuyama et al. (2013) show that productivity and working conditions increased simultaneously in Cambodian garment firms.

The studies of minimum wage mainly discuss the relation of minimum wage policy and employment while hardly focusing on the impact of minimum wage on firm performance. Huang, Loungani, and Wang (2014) find that minimum wage policy increases both profit margins and

employee wages through the study of the PRC market. Evidence suggests that the profitability of the firms may not be worse off with an increasing minimum wage.

The answer to the first part of the question leading this section, then, is in principle quite straightforward. Optimal policies would be those that induce factories to adopt technologies that ultimately improve both working conditions and firm performance. What are these policies? They are policies that induce firms to improve the conditions that are valued by workers so that worker performance increases as a result of the improvements in conditions.

The next part of the question, then, becomes critical. What do workers value? The issue of what changes in conditions has been discussed previously in this report, but it is important to make two additional points. The first is that firms may not know what workers value. Domat et al. (2013) illustrate the mismatch between manager and worker perceptions of what workers value. If managers do not understand what workers want, then it is difficult to design the kinds of improvements that would result in increased effort and thus improve the factories.

The second point has to do with worker perceptions of working conditions. It is possible that workers as a group do not have homogeneous preferences, which makes understanding what workers value more difficult (Pike and Godfrey 2014). One clear example of this has emerged in developing country apparel (and electronics) factories: working hours. There are many examples that suggest that firms have a hard time retaining workers when they follow legal limits on working hours because some workers, especially younger and single workers, want to maximize their earnings while working in the factory. To meet orders, firms may turn to subcontracting, which, in some cases rests in the informal sector and therefore not bound by legal limits on hours (Basole, Basu, and Bhattacharya 2015). Other cases are cited in which firms make overtime compulsory, especially during times of peak demands.

While literature appears on both sides, Golden's (2012) comprehensive review suggests that shorter hours are associated with higher productivity. Flexible schedules not only enhance productivity, but also improve worker health. Healthier workers can reduce labor costs and restrain the hidden cost associated with dissatisfaction and human capital investment. Further, the firm that offers a flexible schedule to their employees has an easier time recruiting new workers and lowers the turnover rate of existing staff.

## VI. TO WHAT EXTENT SHOULD THE DESIGN OF LABOR REGULATIONS INCORPORATE ENFORCEMENT CAPACITY?

There are many factors that help shape HRM policies in developing countries generally and in apparel factories in particular. Labor regulations, especially those set up by domestic governments, play an important role if they are either enforced or internalized into local norms. If local norms do not support improved conditions, labor regulations can help firms coordinate, but only if there is sufficient enforcement capacity.

Sufficient enforcement capacity can be defined in two ways. Kanbur and Ronconi (2016) highlight the importance of the difference between *de jure* regulation, which is the laws “on the books,” and *de facto* regulation, which relates to how well laws are enforced. In many poorer countries, governments do not have enough inspectors. Often inspectors have insufficient training and/or do not have the resources necessary to travel to factories. On the other hand, sufficient enforcement also means having an enforcement system that is fair and is considered to apply the law in a consistent

manner. India recently reformed labor laws to make the inspections more transparent (see Box 3). Many developing countries struggle with weaker-than-optimal institutions and institutional reform broadly is often necessary as a precondition for economic development.

### Box 3: India's Labor Reforms

In late 2014, India announced labor reforms designed to increase the transparency of India's factory inspections. The new program requires that factory inspection reports be loaded to a government website within 72 hours of the visit. The goal is to minimize complaints from business owners who argue that inspections are arbitrary and avoid the "Inspector Raj"—the term given to refer to overregulation by the government of the industry that dates back to Indira Gandhi's economic policies. See <http://www.globalhrlaw.com/resources/labour-law-reforms--india-2014> for more details.

Economic theory helps identify the key variables that would affect any evaluation of the optimal constellation of enforcement regimes and labor regulations that might lead to optimal experimentation. The core of economic theory relies on incentives. Firms will experiment with improvements in working conditions if it is in their interest to do so. One way to affect the firms' incentives is through legislation and regulations that require a certain level of working conditions. Economic theory suggests that firms will follow these regulations as long as the benefit from following regulations are greater than the costs of following them. There are two main sources of benefits.

The first comes from possible improvements in factory performance as discussed earlier. Often, however, firms are unaware of these benefits or they do not have (or, perhaps more importantly, do not think they have) a sufficiently long time horizon to recover the costs. In this case, information sharing may serve as a critical, relatively low-cost way to induce experimentation with improvements in working conditions.

The second source of benefits comes from avoiding punishment for noncompliance. Punishment from noncompliance comes from both the severity of punishment (e.g., the level of fines or amount of prison time) and the probability of being caught (and, if appropriate, convicted). As such, enforcement clearly matters. Ronconi (2010) finds that increased enforcement (as measured by the number of labor inspectors) leads to increased compliance with labor standards. In the absence of effective enforcement, alternatives to domestic regulation emerge. There are many examples. Brien (2013) describes a social labeling program in Australia (Ethical Clothing Australia) that emerged in response to perceptions of insufficient enforcement. Labeling programs such as this are examples of "soft law" that supplement legal obligations, but in the absence of government enforcement capacity their effectiveness often rests on the commitment of factories to participate (Athreya and Campbell 2013). The lack of enforcement leads to a search for alternatives approaches (Berik and van der Meulen Rogers 2010).

Social labeling initiatives are just one example of the kind of system that emerges in the absence of effective enforcement. Wetterberg (2011), for example, focuses on the rise of the Better Factories Cambodia program in the context of insufficient enforcement. This paper, in particular, describes how the Better Factories Cambodia approach took the lack of enforcement into account to forge an alternative multistakeholder approach that has been discussed earlier in this review. One important point from this study is that the multistakeholder approach helps the government improve its enforcement capacity through the cooperation of the various stakeholders.

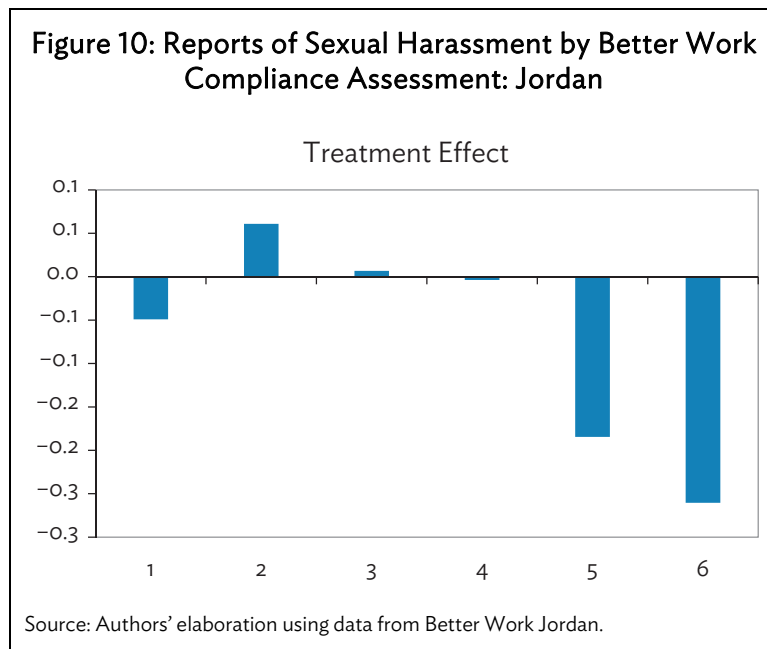
Issues of enforcement have been particularly salient in the area of minimum wages. Groisman (2014) argues that the effectiveness of minimum wages is hard to control. Rani et al. (2013) discuss the coverage and compliance of minimum wage in developing countries based on the survey data from 11 developing countries. These studies show that it is important to find the right combination of policies and interventions so as to achieve effective compliance and therefore support the conventional wisdom that suggests that failure to take enforcement capacity into account would run the risk of implementing standards that may not be reached.

There are several other issues to keep in mind when designing policies that are mindful of effective enforcement. One of these is that enforcement varies by factory size. There have been several studies, such as Almeida and Carneiro (2009), which show that enforcement of labor regulations varies with firm size. As with other enforcement strategies, the benefit–cost ratio leads regulators to target larger firms first, which would affect the cost–benefit analysis each firm would undertake when deciding to improve working conditions. Indeed, Figure 6 shows that compliance is higher for larger firms in Cambodia.

The impact evaluation of Better Work indicates that firms learn from compliance and advisory services and benefit from training. Impact evaluation of interventions related to sexual harassment are particularly indicative. Prior to participation in Better Work, firms were unaware of sexual harassment as a phenomenon in their factories, both in terms of cause and effect. Lin, Babbitt, and Brown (2014) identify organizational norms and misaligned incentives as the fundamental causes of sexual harassment. Further, workers subject to sexual harassment require a compensating pay differential and are less productive as compared to their nonharassed coworkers. The incidence of sexual harassment and firm performance is negatively related. Evidence from Jordan indicates that awareness of sexual harassment, compliance assessments identifying its presence, and training intended to develop organizational norms deterring sexual harassment were effective in reducing its incidence. Initially, reports of sexual harassment increased and decay in beneficial effects occurred. However, by the fifth assessment cycle, reports of sexual harassment had decreased by 20 percentage points.

The impact of Better Work interventions on sexual harassment reports in Jordan is illustrated in Figure 10. Each panel indicates an assessment cycle. As can be seen, after the second assessment cycle, reports of sexual harassment rise. Reports decline at the time of the second and third assessments, but decay occurs in the months following the assessment. However, by the fifth cycle, reports of sexual harassment are 20 percentage points lower than at the first entrance into Better Work, and there is no decay following an assessment.

Developing supervisory skills through Better Work has also been shown to improve productivity and worker job satisfaction, as reported by Babbitt (2016). In a random controlled trial, the positive effects of training on line performance were seen to correct problems with overtime violations. At the end of the study, supervisors trained in the first cohort, exhibited a 22% increase in line productivity.



## VII. CONCLUSIONS: ARE THERE GOOD PRACTICES IN ENFORCING LABOR REGULATIONS/STANDARDS?

One of the main goals of this paper is to identify the factors that would affect the particular constellation of labor regulations and enforcement regimes that are more conducive to experimenting with better labor practices, and, if so, what such a constellation would look like. From the point of view of economic analysis, the optimal constellation generates the “best” result at the lowest cost. This paper defines “best” as that which is most highly valued by the relevant stakeholders: workers, buyers, factory managers, and governments. Since the values of each stakeholder differ across countries, the optimal constellation of policies to improve working conditions will vary across countries. In every country, however, the optimal policy mix should focus on five critical areas:

- (i) working conditions in local context,
- (ii) understanding what stakeholders value,
- (iii) sharing the latest information,
- (iv) optimal legislation and enforcement, and
- (v) minimizing costs of improving conditions.

Labor practices in developing countries tend to be correlated with income per capita in the sense that practices are generally more likely to be considered poor in the poorest countries. While apparel has received a lot of international attention, conditions in the apparel sector are not necessarily worse than they would be in other sectors that apparel workers are likely to work. Poor practices are not unique to the apparel sector; they are often a symptom of development. The logical response is that governments could legislate better conditions. In fact, governments often have legislation that is comparable to that in developed countries. Given limited resources for enforcement, it is important to develop alternative strategies. These alternative strategies should incorporate the concerns of multiple stakeholders. There is a large and growing literature that suggests that programs that bring

together multiple stakeholders and focus on information and learning are likely to be the most successful (Ordor 2014).

One of the leading successful examples has been the Better Work program, which evolved out of the Better Factories Cambodia program (for an interesting history of the development of this program, see Kolben [2004] and Polaski [2006]). The Better Work program has spread to Central America (Bair and Gereffi 2014) and is discussed in depth by World Bank (2015). This program has received much attention in the literature as a multistakeholder alternative to relying on government regulation alone. Early evaluations of the program (e.g., Sibbel and Borrmann 2007 and Shea et al. 2010) suggest that the program enjoyed significant early success in improving compliance. Figure 9, for example, shows that average compliance in Jordan, Viet Nam, and Cambodia increases with the number of Better Work (or Better Factory Cambodia) visits.

In addition to the other discussion about Better Work, it is important to point out that one of the strengths of the program is that it has the potential to save factories money through reduced inspections. By having the ILO support the monitoring, factories that support the program can choose to accept the ILO monitoring reports instead of performing their own audits. The reduction of monitoring represents potential savings for the factory.

The success of the Better Work program has resulted in the spread of the Better Work model to other countries. Better Work now operates in Cambodia, Lesotho, Haiti, Nicaragua, Indonesia, Bangladesh, Viet Nam, and Jordan. While there are other programs that can point to important successes, the Better Work model seems to be one that is likely to expand significantly in scope.



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## **Working Conditions, Work Outcomes, and Policy in Asian Developing Countries**

Working conditions in developing countries are the focus of policy makers and stakeholders in Europe, the Americas, and especially Asia. In this debate, the garment sector has perhaps captured the most attention. This paper reviews academic studies of the causes and consequences of poor conditions in developing country garment factories with a special emphasis on causes and potential solutions for South Asia.

### **About the Asian Development Bank**

ADB's vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries reduce poverty and improve the quality of life of their people. Despite the region's many successes, it remains home to half of the world's extreme poor. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.



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